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BEFORE THE ARIZONA CORPORATION COMMISSION

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Commissioner

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Commissioner

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IN THE MATTER OF THE APPLICATION OF) DOCKET NO. E-10345A-98-0473
ARIZONA PUBLIC SERVICE COMPANY FOR)
APPROVAL OF ITS PLAN FOR STRANDED)
COST RECOVERY.)

IN THE MATTER OF THE FILING OF ARIZONA) DOCKET NO. E-10345A-97-0773
PUBLIC SERVICE COMPANY OF UNBUNDLED)
TARRIFS PURSUANT TO A.A.C. R14-2-1602 ET)
SEQ.)

IN THE MATTER OF THE COMPETITION IN) DOCKET NO. RE-00000C-94-0165
THE PROVISION OF ELECTRIC SERVICES)
THROUGHOUT THE STATE OF ARIZONA.) **NEV SOUTHWEST, L.L.C.'S**
) **COMMENTS REGARDING**
) **ARIZONA PUBLIC SERVICE**
) **COMPANY'S APPLICATION FOR**
) **APPROVAL OF SETTLEMENT**
) **AGREEMENT**

NEV Southwest, L.L.C. ("NEV Southwest"), through undersigned counsel, and pursuant to the Procedural Order dated May 25, 1999, hereby submits these comments concerning Arizona Public Service Company's ("APS") Settlement Agreement dated May 17, 1999 ("Settlement Agreement") in the dockets captioned above. In support hereof, NEV Southwest states as follows:

NEV Southwest concurs with APS that there are substantial benefits to the public as a result of the Settlement Agreement. In particular, Commission approval of the Settlement Agreement will enable competition to begin sooner in APS' service territory than if these issues were resolved through hearing and litigation. NEV Southwest was not a party to the negotiations

1 that resulted in the Settlement Agreement. Accordingly, NEV Southwest submits these
2 comments to enhance the Settlement Agreement and to provide the Commission with a more
3 solid basis upon which to approve a settlement of the matters related to these consolidated
4 dockets.

5 **I. ARTICLE I - IMPLEMENTATION OF RETAIL ACCESS.**

6 NEV Southwest supports Article I as proposed.

7 **II. ARTICLE II - RATE MATTERS.**

8 **A. 2.1 Unbundled Rates.**

9
10 APS has approached unbundled rates and stranded costs from a bottom-up approach, as
11 opposed to a market generation credit method. In this approach, separate unbundled charges are
12 developed for various components of electric service including distribution, metering, meter
13 reading, billing, transmission, ancillary services, system benefits, and the charge for stranded
14 cost (CTC). The embedded generation charge (above stranded cost) is not computed directly,
15 but is derived by subtracting the sum of all the other charges from the total standard offer rate.
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17 NEV Southwest is not opposed to APS' bottom-up approach. NEV Southwest
18 recognizes that APS' approach may have some advantages over a market generation credit
19 method, and is ultimately how electric bills will be computed when the CTC and standard offer
20 rates are eliminated in the future. However, under APS' approach, the embedded generation
21 charge is essentially a residual (not computed directly) and should be reviewed to ensure that it is
22 reasonable.
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24 Such review is important because the residual generation charge will determine the
25 potential savings for any customer who chooses to access the competitive market. In other
26 words, the potential savings from competition is the residual generation charge compared with
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1 the generation price that a competitive supplier will offer. This competitive price will include the
2 competitive wholesale generation cost plus a margin to cover additional costs and return.

3 If the potential savings are at least moderate, then more customers should be enticed to
4 choose other providers, and the electric market in Arizona will be susceptible to competition. If
5 the potential savings are low or negative then few customers will choose a competitive provider
6 and the competitive electric market in Arizona will flounder.

7 The Salt River Project implemented a similar approach to generation costs, but did not
8 perform or provide an analysis of the potential effects on customer savings. As a result, an
9 approach was approved with potential competitive savings for some customers that appear to be
10 very low or even negative. This suggests several potential problems: (1) the CTC was
11 improperly set due to incorrect assumptions about the future competitive market price; (2) other
12 unbundled components were improperly valued; and (3) historic allocations of generation costs
13 were too low for a particular rate class, which would result in low or negative stranded costs for
14 that class. It appears that SRP's problems occurred with both the CTC assumptions and historic
15 class allocations of generation costs. As a result, it seems that there is low potential for near term
16 participation in competitive electric market in the SRP territory. In fact, to NEV Southwest's
17 knowledge, no SRP customers have switched to competition, even though the SRP territory has
18 been opened to competition.
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21 NEV Southwest believes that the Commission should avoid a similar mistake in the APS
22 territory. In the proposed Settlement Agreement APS has not presented any analysis of the
23 residual embedded generation charge for the various rate classes compared with competitive
24 prices that are likely to occur. NEV Southwest recommends that APS perform this analysis and
25 provide the results to Staff and the parties.
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1 NEV Southwest also has several concerns about specific rate tariffs included in Exhibit A
2 of the Settlement Agreement. First, NEV Southwest believes that the On-Site Generation
3 provision of the Direct Access General Service tariff (DA-GS1) is premature. The Commission
4 has initiated action on this, and these issues should be addressed by the Commission before this
5 tariff provision is approved. Until then, NEV Southwest recommends that this provision be
6 removed from the tariff.

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8 Furthermore, NEV Southwest is concerned about the credits for ESP metering, meter
9 reading, and billing proposed in the Direct Access Tariffs. Admittedly, NEV Southwest has not
10 conducted a detailed study on this specific issue; however, it appears from the analysis that it has
11 conducted that the credits are too low and are not equal to the concomitant charges in the
12 standard offer tariffs. Consequently, NEV Southwest is concerned that competitive customers
13 will not receive a credit equal to APS' cost of providing these services as reflected in the
14 standard offer tariffs.

15 **B. 2.2 Rate Decreases.**

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17 Near-term decreases in standard offer rates are not necessarily a benefit of competition,
18 but rather a reflection of declining utility costs, aging rate bases, and potential over-earning.
19 They could occur without competition. NEV Southwest, however, is aware that decreases in
20 standard offer rates are contemplated (but not mandated) in the pending Competitive Rules.
21 Nevertheless, NEV Southwest is concerned that APS' proposed standard offer rate decreases
22 may be too aggressive and may not be conducive to a competitive market. Standard offer rate
23 decreases may be desirable to extend benefits to customer classes (such as residential and low
24 income) that are not likely to benefit from competition in the near term. However, that benefit
25 would not be necessary for commercial and industrial customers for whom the competitive
26 market will be a viable option.
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1 Furthermore, if the competitive market were not a viable option for commercial and
2 industrial customers, it would mean that the residual generation charge was too low, and that
3 APS' unbundled charges and stranded cost recovery were improperly set. Therefore, NEV
4 Southwest recommends that APS reduce the proposed standard offer rate decrease for
5 commercial and industrial customers and apply the savings towards some mechanism which
6 would increase the potential savings for direct access customers. This would have the dual
7 benefit of keeping APS' earnings at proper levels and also stimulating the launch of the
8 competitive market in Arizona.
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10 **C. 2.3 Return to Standard Offer.**

11 The Settlement Agreement proposes that customers above 3 MW must provide one-
12 year's notice to return to standard offer service. NEV Southwest believes that this is
13 inappropriate and should be excluded from the Settlement Agreement. APS may have a concern
14 that returning customers may cause unexpected burdens to APS' energy procurement
15 requirements. However, APS does not require new industrial customers who are moving into
16 APS' service territory to give notice before commencing service, even though they might create
17 a similar burden. A better solution for this would be to discontinue standard offer service for all
18 customers greater than 3 MW after 2001.
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20 APS may also be concerned that competitive customers could switch back to standard
21 offer service during the summer months when competitive market prices may be high. NEV
22 Southwest recommends that this concern be addressed by discontinuing future standard offer
23 service as mentioned above, or by allowing customers to switch back to standard offer only once
24 per year.
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D. 2.6 Adjuster Clause.

NEV Southwest believes that the use of an adjuster mechanism to defer transitional costs does not appear to be compatible with the rate reductions proposed in the Settlement Agreement. On one hand, APS is suggesting that reduced costs can accommodate near term rate reductions. On the other hand, APS is requesting deferred cost recovery for increased near term costs, including a return on (apparently) both capital and operating costs. NEV Southwest requests the Staff to assess this issue and recommends that the utility costs be handled in standard rate procedures rather than the adjuster mechanism proposed in the Settlement Agreement.

III. ARTICLE III - REGULATORY ASSETS AND STRANDED COSTS.

The Settlement Agreement guarantees APS full recovery of \$350 million of stranded costs through the adjuster mechanism. NEV Southwest does not necessarily oppose this amount. However, the Settlement Agreement should properly reflect that this recovery is a guarantee and not a "reasonable opportunity to recover" this amount. *See* Section 3.3 of the Settlement Agreement. In addition, NEV Southwest requests that APS provide Staff and the parties the key inputs and assumptions from the stranded cost calculation. In particular, Staff should review the assumed market price, which underlies the calculation.

IV. ARTICLE IV - CORPORATE STRUCTURE.

NEV Southwest believes it is APS' intent to establish the generation affiliate under Pinnacle West, not under APS. NEV Southwest also believes that APS intends to procure generation for standard offer customers from the wholesale generation market as provided for in the pending Competition Rules. The affiliate generation company could bid for APS' standard offer load under an affiliate FERC tariff, but there would be no automatic privilege outside of this market bid. NEV Southwest supports these concepts and recommends that they be explicitly stated in the Settlement Agreement. This concern also applies to the relationship among APS,

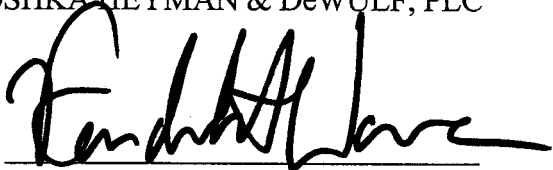
1 the affiliate generation company, and APS Energy Services, (APS' competitive marketing
2 affiliate). NEV Southwest recommends that APS file an affiliate tariff at FERC to accommodate
3 the transactions among APS, the affiliate generation company, and APS Energy Services.

4 **V. CONCLUSION.**

5 NEV Southwest supports the settlement process and requests that the issues addressed
6 herein be resolved in a timely manner.

7 RESPECTFULLY SUBMITTED this 25th day of June, 1999.

8 ROSHKA HEYMAN & DeWULF, PLC

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10
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1 **Original and ten copies of the foregoing**
2 **filed this 25th day of June, 1999 with:**

3 Docket Control
4 ARIZONA CORPORATION COMMISSION
5 1200 West Washington Street
6 Phoenix, Arizona 85007

7 **Copy of the foregoing hand-delivered**
8 **this 25th day of June, 1999 to:**

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